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SUBJECT: NETHERLANDS: GLOOMY ECONOMIC INDICATORS GENERATE PARLIAMENTARY DEBATE

Ref: A. THE HAGUE 910, B. THE HAGUE 981

THE HAGUE 00001018 001.2 OF 002

¶1. (U) SUMMARY: The Netherlands' leading statistical agency forecasts a recession in 2009 and only slight GDP growth of 1.0 percent in 2010. Although the Netherlands likely will weather the economic crisis better than many of its EU neighbors, it still faces rising unemployment and significant declines in trade and investment. The expected government budget surplus in 2009 has disappeared, to be replaced by a deficit of 1.2 percent of GDP in 2009 and 2.4 percent in 2010. The rising deficit predictions prompted heated debate December 10 as Prime Minister Jan Peter Balkenende and his cabinet defended their economic policies before parliament. While some parliamentarians called for new government measures now to offset the impending deficit, Balkenende advocated staying the course until the effects of the government's recent interventions in the financial sector and economic stimulus package could be evaluated. End summary.

GLOOMY ECONOMIC INDICATORS

¶2. (U) The Netherlands Bureau for Economic Policy Analysis (CPB) released a gloomy forecast December 10 that predicts shrinking international trade, rising unemployment, a growing budget deficit, and recession in 2009 - the first annual shrinkage of the Dutch economy since 1982. Following are the key elements of CPB's forecast:

-- GDP: Dutch GDP is expected to shrink by 0.75 percent in 2009 (compared to 2.25 percent growth in 2008), but a modest recovery of trade and credit markets beginning in the second half of 2009 should produce GDP growth of 1.0 percent in 2010.

-- Unemployment: 2009 will see an end to a period of three years of decreasing unemployment. This year's level of 4.0 percent will rise to 4.5 percent in 2009 and 6.5 percent in 2010. The number of unemployed will rise from 300,000 in 2008 to 500,000 by the end of ¶2010. Given the currently low level of unemployment, however, CBP predicts that the labor market will remain tight deep into 2009.

-- Inflation: Inflation is expected to fall sharply, from 2.5 percent in 2008 to 1.5 percent in 2009 and 1.0 percent in 2010. This drop is due mainly to lower prices of oil and raw materials.

-- Trade: International trade, the cornerstone of the Dutch economy, will be hit hard by the deteriorating international situation, but CBP expects it to improve quickly in 2010. Exports

of goods (excluding energy) will decline from 7.3 percent growth in 2007 to 2.75 percent in 2008. Exports will shrink by 2.25 percent in 2009, but rebound quickly to 3.0 percent growth in 2010. Although the price competitiveness of Dutch exports will improve because of the recently depreciated euro, the overall decline in exports will offset this advantage. Meanwhile, imports will shrink by 2.5 percent in 2009 but grow by 1.5 percent in 2010, compared to 5.75 percent growth in 2008.

-- Business investment: Although the volume of business investments grew in 2008, it is expected to decline sharply in 2009 and 2010. Weak demand and reduced production will offer little reason to invest in new machinery, while lower profits will reduce returns on investment. The tighter credit market also will make financing new investment more difficult.

-- Purchasing power: Purchasing power will improve, from zero
Q-- Purchasing power: Purchasing power will improve, from zero
growth in 2008 to 1.75 percent growth in 2009, but only 0.25 percent in 2010. Several factors contribute to this increase, including lower inflation, declining oil prices, the Dutch government's decision not to require employees to pay unemployment insurance contributions as of 2009, and collective bargaining agreements (concluded earlier in 2008 when inflation was expected to rise) that provide for an overall wage increase of about 3 percent.

-- Government budget: The Government of the Netherlands (GONL) will enjoy a budget surplus of 1.3 percent in 2008. Before the full onset of the financial crisis in September, CBP had predicted a 2009 surplus of 1.2 percent. That has now transformed into a projected budget deficit of 1.2 percent in 2009 and 2.4 percent in 2010. Primary contributors to this downturn are substantially lower tax revenue, higher expenditure on unemployment benefits, and declining natural gas profits.

PARLIAMENT DEBATES NEXT STEPS

¶3. (U) CBP's predictions generated a heated, albeit largely theoretical, parliamentary debate December 10 about what steps should be taken if the budget deficit threatens to rise above 2.0 percent. The terms of the agreement governing the ruling tri-party coalition call for immediate government measures if the deficit exceeds that level. Such measures likely would include cuts to existing government programs or tax hikes to increase government revenue. Some parliamentarians, including members of Prime Minister Balkenende's Christian Democratic Alliance (CDA) party, argued that the terms of the coalition agreement must be strictly honored. Liberal Party (VVD) members asserted that budget cutbacks should be made now to offset a growing deficit, pointing to the GONL's foreign development assistance budget (currently 0.8 percent of GDP) as a prime target for reduction. The general consensus, however, was that the GONL had taken correct actions to date to stimulate the economy, and no spending cuts should be considered at this early stage.

¶4. (U) For their part in the debate, Prime Minister Balkenende, Finance Minister Wouter Bos, and Economic Affairs Minister Maria van der Hoeven advocated patience in evaluating how the Dutch economy was responding to recent GONL stimulus efforts. Minister Bos's Labor Party (PvdA) largely agreed with this approach, arguing that the coalition agreement was not sacrosanct and flexibility was needed in these unprecedented economic times. Since September, the GONL has extended bank deposit insurance, guaranteed new bank loans, nationalized the Dutch holdings of Belgian conglomerate Fortis, and provided total capital injections of over 30 billion euro to needy Dutch banks (ref A). Meanwhile, the GONL's 6 billion euro economic stimulus package has introduced corporate tax breaks, shorter working hours and corresponding unemployment benefits, and accelerated infrastructure projects to stimulate job growth (ref B). Balkenende cautioned against the GONL changing course too quickly until the results of these interventions in the economy could be evaluated. He asserted that the current GONL budget was appropriate

and should not be amended until the start of the regular 2010 budget cycle in spring 2009 - a conclusion with which most parliamentarians agreed.

COMMENT

¶5. (SBU) Comment: The CBP is the Netherlands' most respected statistical agency, and its predictions have hit home the bleak economic reality that the country likely will endure over the next two years. Despite looming recession, the Netherlands nonetheless is expected to fare better than many of its EU neighbors; CBP predicts GDP shrinkage of 1.0 percent in the Eurozone in 2009, for example, compared with only -0.75 percent in the Netherlands. The agreement among Balkenende and his cabinet ministers - in particular Finance Minister Bos - on the need for patience in evaluating next steps in the economic crisis is noteworthy. Fierce rivals in the November 2006 national election, Balkenende and Bos have coordinated closely on how to handle the crisis and presented a confident, unified front - to the general praise of the Dutch public. As the economy declines, businesses suffer, and unemployment rises,
Qeconomy declines, businesses suffer, and unemployment rises,
however, public criticism of GONL action is likely to increase. The goodwill that Balkenende and his cabinet have enjoyed since September likely will erode. End comment.

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